

REGULAR MEETING

SUBJECT: Update on Federal Legislation

ITEM NUMBER: 7b

ATTACHMENT(S): 1

ACTION: X

DATE OF MEETING: August 5, 1998

INFORMATION:

PRESENTER: Ms. DuCray-Morrill

Attached is a comprehensive report from Hogan & Hartson on issues at the federal level. Ms. DuCray-Morrill will provide a verbal presentation at the meeting.

**MEMORANDUM FOR
THE CALIFORNIA STATE TEACHERS' RETIREMENT SYSTEM**

Washington Monthly Report

After having spent much of the first part of this month out of session with the July 4 recess, Congress returned to a crowded agenda of appropriations bills to be acted upon between now and the month-long August break. With a target adjournment date of October 9 in this election year-shortened session, September promises to be a frenetic month, as Congress struggles to complete action on all 13 appropriations measures, send to the President a significant tax cut package, and act on other politically sensitive legislation such as reform of managed care. The partisan nature of the fray is likely to intensify, as each side pursues an agenda and offers proposals aimed at scoring political points with the voters.

The outlook for Federal budget surpluses and the appropriate use of such surpluses will drive the debate over tax cuts. The President very effectively outflanked Congressional GOP leaders earlier this year by stipulating that any budget surpluses must first be applied toward restoring the long-term solvency of Social Security, before any tax cuts can be contemplated. Efforts to apply the projected surpluses to tax relief had been criticized on the ground that once the surpluses accumulating in the Social Security trust fund were disregarded, a deficit remained in the Federal government's operating budget. Then the notion of a "surplus

In its July 15 budget outlook update, the Congressional Budget Office, projecting ongoing surpluses over the next decade, now estimates that beginning five years from now in fiscal year 2004 and for the next five years thereafter, the Federal operating budget will be in surplus even after the Social Security surpluses are disregarded.

This "surplus surplus" has renewed calls by the Congressional GOP leadership to apply these "surplus surpluses" to fund major tax cuts. The President, for his part, has continued to stress Social Security solvency. While Congressional Republicans are unlikely to repeat the government shutdown mistake by holding out for harsh spending cuts in the appropriations side, Congress and the President could well be headed for a showdown in September over major tax cuts. The House GOP leadership in particular expects to send major tax cut legislation to the President with the goal of forcing him to sign GOP-authored tax cuts into law or wield a Democratic President's veto pen with respect to tax relief. The House GOP leadership is considering phasing out the so-called "marriage penalty" in which a married couple pays a higher effective tax rate than two unmarried wage-earners; cutting the top individual capital gains tax rate to 15 percent; phasing out the estate tax; repealing the increased tax on Social Security benefits that had been proposed by President Clinton in 1993; reducing or eliminating the penalty under Social Security for those who work past 65; and greater deductibility of health insurance premiums for the self-employed.

As this partisan budget free-for-all proceeds, the oft-quoted remark of the late Sen. Everett Dirksen (R-Ill.) is likely to reappear, that "a billion here, a billion there, and pretty

Mandatory Social Security

We are following up on the statement STRS filed with the House Ways and Means Social Security Subcommittee and are coordinating with the State and local government group coalition on mandatory coverage, now termed the Coalition to Preserve Retirement Security.

The near term aim of the coalition continues to be establishing and mobilizing a strong grassroots network of State and local government groups, employers, and employees in key States. Coalition members are fanning out in their respective States to educate employers about the cost impact and employee groups about the prospect of benefit cuts and loss of control over the setting of benefits. It has become clear that a sizable education effort is necessary within the coalition's own ranks to mobilize those affected States that have not yet become active and to mobilize employer and employee groups at the grassroots level in those States that already are participating in the coalition.

Our sense from afar in Washington is that in many States, including California, the reality and immediacy of the mandatory coverage threat simply has not percolated down to the local employer and employee group level to those leaders who would be best situated to speak to their Members of Congress about cost burden, benefit cuts, and disruption.

The employee groups for teachers, both nationally and in California, appear to have focused much of their attention on pursuing Federal legislation to alleviate the impact of the so-called "offsets" that reduce Social Security benefits of State and local government retirees or their spouses who receive public pensions. These offsets do indeed have an untoward impact on a significant number of State and local retirees, particularly those at the lower-income levels. However, Congressional proponents of mandatory coverage counter that mandatory coverage of new hires offers the most complete solution to the offset problem for the future by bringing these State and local workers into the Social Security system as full freight-paying members. Accordingly, the efforts of the employee groups focused on alleviating the offset problem should not come at the expense of mounting a vigorous grassroots effort over the next three to four months to communicate vehement opposition to mandatory coverage to their Members of Congress and to the President.

Similarly, it is important that employer groups and local school districts communicate at the grassroots level with Members of Congress about the disruptive cost effect that mandatory coverage would have on struggling school budgets. Such a theme is likely to have appeal to Members of Congress from both parties. As noted in previous reports, Members of Congress from both parties who advocate reform of Social Security through some version of personal investment accounts view mandatory coverage as an attractive source of near-term cash to help fund the Social Security system until the revenues being diverted to personal accounts

can compound into meaningful amounts. It is important to dispel the notion among many of these reformers that mandatory coverage is some cost-free "no brainer," in the words of one White House staffer, that at worst raises transition issues for State and local governments that can be managed over a several-year period. An effective way to counter this myopic view is to demonstrate the immediate adverse impact on local government budgets for education and other essential government services.

We will continue to coordinate with STRS staff, the coalition, and the CalPERS representatives in Washington as this effort moves forward to mobilize strong grassroots activity in as many of the key non-Social Security States as possible.

Elk Hills Compensation

The House version of the Defense Authorization Act that eliminates the appropriation requirement for payment of the Elk Hills compensation to the State has now gone to a House-Senate Conference to resolve the various differences with the Senate version of the Act which has no Elk Hills provision.

We have been working very closely with our long-time champion Rep. Bill Thomas (R-Bakersfield) seeking to have the House Elk Hills provision included in the final version of the legislation. In the early going, there has been some resistance in some quarters on the Senate side -- particularly at the staff level -- to striking the Elk Hills appropriations requirement as the House provision would do.

In the original Elk Hills compensation legislation, the Senate had been resistant to settling California's claim legislatively, with the Senate wishing to set the funds aside and require the State to try to negotiate a settlement with the Administration. The then-chief Senate negotiator Sen. John McCain (R-Ariz.) -- who had suggested the escrow and negotiation approach as a compromise in the original legislation -- also had insisted that payment from the escrow fund be subject to an appropriation. Of course, that was before Congress adopted harsh budget caps in subsequent budget legislation that made it very difficult to adopt any new appropriation spending item without cutting a commensurate amount from some other program.

Rep. James Inhofe (R-Okla.) has taken over Senator McCain's responsibility for the Elk Hills portion of the Defense Authorization, although Senator McCain reportedly has continued to express the view that the appropriation requirement should remain in the statute -- apparently on the basis principally that "a deal's a deal." (In addition, the Elk Hills compensation would count as mandatory spending which must be offset by a mandatory spending reduction somewhere else in the budget.) Attorney General Lungren has written a strong letter of support for Elk Hills compensation to Senator Inhofe (attached), stressing that the State has held up its part of the settlement and that it is now time for the Federal government to follow through on its obligation to compensate the State.

Thus far, the House negotiators have stood firm in support of the House provision striking the appropriations requirement, arguing that the settlement has been reached, the land

has been sold, the money has been set aside, and hence why not just give to the State in accordance with the seven-year installment schedule set forth in the settlement agreement.

At this juncture, it seems that the fate of the Elk Hills provision in the House-Senate Conference on the Defense Authorization Act will hinge on Member-level discussions led by Rep. Thomas (and other key Members of the California delegation where useful).

Securities Litigation Reform Legislation

Legislation to curtail the use of State law and State courts for class actions securities fraud claims involving publicly-traded companies will be moving shortly to a House-Senate Conference to resolve the differences between the House (H.R. 1689) and Senate (S.1260) versions.

The Senate already has adopted its version of the legislation, and the full House is scheduled this week to approve the House counterpart under an abbreviated procedure used to consider noncontroversial measures.

Among the items to be resolved in the House-Senate Conference is the final drafting of a provision that would preserve the rights of State and local governments and their pension plans to bring class actions securities fraud claims under State law.

John S. Stanton

Attachment
July 20, 1998